



Reference: AUD-7-1: 31 (0581 /03)

Date: 24 April 2003

To: Mr. Benon Sevan, Executive Director
Office of the Iraq Programme

From: Esther Stern, Director
Internal Audit Division, OIOS

Subject: **OIOS Assignment No. AF2003/98/1: Preliminary review of procedures to amend "Oil-for-food" Programme contracts pursuant to Security Council Resolution 1472(2003)**

1. In order to assist the Office of the Iraq Programme (OIP), OIOS is providing its observations and recommendations on procedures being established by OIP's Contract Processing and Monitoring Division (CPMD) for the amendment of the contracts and authorization of additional payments under the "Oil-for-food" Programme, as called for by Security Council Resolution 1472 (2003). Accordingly, discussions were held with OIP on 14 April 2003 relating to procedures being established and certain additional documents were reviewed, with the view of ensuring that the interests of Organization are properly safeguarded and that the resulting amendments and authorizations will be consistent with the UN Financial Regulations and Rules. OIOS is pleased to note that OIP has already taken steps to modify some of its procedures as a result of these preliminary discussions.

2. The draft report was shared electronically with OIP on 17 April 2003 and their response obtained on 23 April 2003. The comments of the OIP are indicated in *italics* in the report. OIOS appreciates OIP's quick response to the recommendations. Based on the response, OIOS is withdrawing recommendations 1 to 3 and closing recommendation 4 in its database.

Introduction

3. In view of the exceptional circumstances prevailing in Iraq, the Security Council adopted Resolution 1472 (2003) on 28 March 2003, which called for certain technical and temporary adjustments to the "Oil for Food" Programme to ensure the implementation of the approved contracts concluded by Government of Iraq (funded and non-funded). Approximately \$10 billion worth of supplies were in the production and delivery pipeline at the time the Resolution 1472 was adopted.

4. The Resolution authorized the Secretary-General or his representatives, inter-alia, to (i) establish alternative locations within or outside Iraq for the delivery, inspection and authentication of supplies; (ii) redirect the shipment of goods to relevant locations; (iii) prioritize those funded and non-funded contracts which can be fulfilled within a 45-day period of the resolution's mandate; (iv) proceed with these contracts in accordance with such established priorities; (v) negotiate and agree

on necessary adjustments in the terms and conditions of these contracts and their respective letters of credit (LOC); and (vi) use SCR 986 funds to compensate suppliers and shippers for agreed additional shipping, transportation and storage costs incurred as a result of diverting and delaying shipments, subject to the procedures decided by the 661 Committee on the recommendations of OIP.

5. In response to these developments, OIP has been working on the various issues involved. OIP and the other UN Agencies administering "Oil-for-food" Programme contracts have prepared a list of contracts for goods that are considered possible immediate priorities in view of the present circumstances. The office has also identified a list of 505 contracts, under which goods were in transit to Iraq as of 17 March 2003 (the date the independent inspection agents (Cotecna) were withdrawn from Iraq). The list indicates that goods with a pending shipment value of approximately US\$ 2.12 billion were in transit.

6. Some of the contracts, for which the goods were in transit and identified as a priority, have been "adopted" by the UN Agencies (146 contracts with a pending shipment value of \$1.14 billion). For these contracts, it will be the responsibility of the UN Agencies to contact the suppliers to establish the locations to which the goods may be diverted and make the necessary amendments to the contracts. For those contracts relating to goods in transit, which were not adopted by UN Agencies (359 contracts with a shipment value of \$983.4 million), OIP will be responsible for any required contract amendments.

Findings and recommendations

7. In OIOS's view, OIP is not in the best position in terms of procurement/contract negotiations skills and expertise needed to negotiate the required contract amendments, even though they have technical knowledge of the contracts. Moreover, CPMD, which is primarily staffed with customs experts, does not have expert staff trained in UN procurement procedures. There is therefore a need for UN procurement staff to be assigned to CPMD to ensure the successful completion of the required tasks. Additionally, the custom experts at CPMD are consultants and not UN staff, and thus could not be delegated contact signing authority. Given this situation, OIP should consider bringing the UNOHCI Procurement Officer to New York on a short-term basis to assist with the urgent tasks.

8. Furthermore, OIOS is of the opinion that the amendment of contracts is essentially a procurement function involving financial commitments on behalf of the Organization. Under the Procurement Manual and the Financial Regulations and Rules, only officials authorized by the Assistant Secretary-General, Office of Conference and Support Services and the UN Controller may enter into contractual commitments, unless an exception is granted in writing by the Under-Secretary-General, Department of Management. In addition, at United Nations Headquarters, this authority resides in the Procurement Division, OCSS. OIOS is also concerned that OIP has not established an adequate segregation for its staff involved in this process. For example, individual CPMD customs officers are responsible for negotiating contract amendments, approving the amendments, in addition to monitoring functions.

9. In order to meet the tight deadlines established by the Security Council (i.e. 45 days from the date of the resolution's adoption), OIP has taken certain steps including: (i) identifying contracts that

need to be amended; (ii) sending questionnaires to the suppliers; (iii) developing templates for amending existing contracts; (iv) issuing instructions to UN Agencies for amending contracts they have adopted; and (v) consulting with the UN Treasury on modifications that may be required to the Letters of Credit. In addition, 137 contracts with a shipment value of \$395 million were identified as possible priority contracts under which goods could be shipped within the 45-day timeline, and related instructions to CPMD staff for handling the amendments to the contracts are being drafted.

10. Furthermore, procedures for the amendment of contracts have been decided by the Committee established pursuant to the SCR 661 (1990). These procedures state that negotiations with the suppliers shall be conducted in accordance with established UN procurement procedures.

Recommendations

OIOS recommends that the Office of the Iraq Programme:

- (i) Immediately obtain a formal authorisation or exemption (delegation of procurement authority) from the USG/DM and the UN Controller to enable it to enter into negotiations and amend the contracts under the "Oil for food" programme, in view of the exigent circumstances (AF03/98/1/001);
- (ii) Request formal assistance from the Procurement Division and OLA in negotiating and amending the contracts, including the assignment of necessary staff in view of the limited expertise available in OIP. OIP should also consider the temporary relocation of the UNOHCI Chief Procurement Officer to OIP to assist with the exercise (AF03/98/1/002);
- (iii) Ensure that any changes/amendments to the contracts are consistent with the UN Financial Regulations and Rules and that any additional payments authorised are reasonable and are supported by appropriate documentation such as third party invoices etc. (AF03/98/1/003); and
- (iv) Issue comprehensive guidelines to the UN Agencies for amending contracts adopted by these Agencies with emphasis on following established procurement procedures consistent with the UN Financial Regulations and Rules (AF03/98/1/004).

11. *In their response to recommendation 1 to 3, OIP informed OIOS that while sharing the concern of OIOS in connection with renegotiation of contracts not adopted as priority contracts by UN Agencies, OIP fully concurred with OIOS findings that consultants within OIP should not be tasked to perform this function. They further stated that for this reason they sought the advice and assistance of PD and OLA and were advised that it should be the UN Agencies and Programmes that shall negotiate with the suppliers of goods in transit regarding the necessary adjustments in terms*

and conditions of the contracts including adjustments in the contract price. Accordingly, OIP informed (18 April 2003) the Heads of Agencies and Programmes concerned that while OIP is poised to assist by performing all possible data gathering and analytical work, the negotiations and amendments should be performed by the relevant UN Agencies and Programmes. OIP stated that this measure addresses the OIOS's concerns and renders recommendations 1 to 3 as not necessary. Based on the clarifications now provided after receiving PD and OLA advice, OIOS is withdrawing recommendations 1 to 3.

12. In relation to recommendation 4, OIP stated that following consultation with UN Treasury and OLA, they had issued guiding procedures to the UN Agencies to assist them in processing amendments to the contracts in conjunction with their established procurement procedures. Based on the clarification and documentation provided by OIP, OIOS is closing recommendation 4.

13. I thank you and the staff of OIP for the cooperation and assistance provided to the auditors.

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